



**Washington State Auditor
Brian Sonntag**

INDEPENDENT AUDITOR'S REPORT

July 19, 2011

Council and Executive
King County
Seattle, Washington

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund and the aggregate remaining fund information of King County, Washington, as of and for the year ended December 31, 2010, which collectively comprise the County's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the County's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the Building Development and Management Corporations fund which represent 10 percent, -0.9 percent and 2 percent, respectively of the assets, net assets and revenues of the governmental activities, and 5 percent, -0.5 percent and 0.2 percent, respectively, of the assets, net assets and revenues of the aggregate remaining fund information. We did not audit the financial statements of the Water Quality Enterprise Fund, a major fund, which additionally represents 67 percent, 25 percent and 27 percent, respectively, of the assets, net assets and revenues of the business-type activities. We also did not audit the financial statements of the Public Transportation Fund, a major fund, which additionally represents 27 percent, 65 percent and 60 percent, respectively, of the assets, net assets and revenues of the business-type activities. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Building Development and Management Corporations, the Water Quality Enterprise and Public Transportation funds, is based on the report of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The financial statements of the Building Development and Management Corporations, Water Quality Enterprise and Public Transportation funds were not audited in accordance with *Government Auditing Standards*. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of the other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the reports of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component

units, each major fund and the aggregate remaining fund information of King County, Washington, as of December 31, 2010, and the changes in financial position and, where applicable, cash flows thereof, and the respective budgetary comparison for the General and Public Health funds for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 1, during the year ended December 31, 2010, the County implemented Governmental Accounting Standards Board Statement 51, *Accounting and Financial Reporting for Intangible Assets*.

In accordance with *Government Auditing Standards*, we will also issue our report dated July 19, 2011, on our consideration of the County's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. That report will be issued under separate cover in the County's Single Audit Report. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis on pages 3 through 17, condition assessments and preservation of infrastructure eligible for modified approach on pages 116 through 118, and postemployment health care plan on page 118 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We and the other auditors have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the County's basic financial statements. The accompanying information listed as combining and individual fund statements and schedules and supplementary information on pages 119 through 174 is presented for purposes of additional analysis and is not a required part of the basic financial statements. This information has been subjected to auditing procedures applied in the audit of the basic financial statements and, in our opinion, based on our audit and the report of the other auditors, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

The information identified in the table of contents as the Introductory and Statistical Sections is presented for purposes of additional analysis and is not a required part of the basic financial statements of the County. Such information has not been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, accordingly, we express no opinion on it.

Sincerely,

A handwritten signature in black ink, appearing to read "Brian Sonntag", written in a cursive style.

BRIAN SONNTAG, CGFM
STATE AUDITOR

MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)

This section of King County's Comprehensive Annual Financial Report (CAFR) presents a narrative overview and analysis of the financial activities of the County for the year ended December 31, 2010. We encourage readers to consider this information in conjunction with that furnished in the letter of transmittal, which can be found preceding this narrative, and with the County's financial statements and notes to the financial statements, which follow.

FINANCIAL HIGHLIGHTS – PRIMARY GOVERNMENT

- As of December 31, 2010, the assets of the County exceeded its liabilities by \$4,415.3 million (net assets). Because most of the County's net assets are either invested in capital assets or restricted as to use, the combined unrestricted net assets was \$188.0 million at the end of the year.
- In 2010, the County's total net assets increased by 2.5 percent (\$108.9 million). The governmental net assets increased by 3.4 percent (\$73.7 million), and the business-type net assets increased by 1.6 percent (\$35.2 million).
- As of December 31, 2010, the County's governmental funds reported combined ending fund balances of \$565.4 million. Approximately 80.3 percent (\$453.9 million) is unreserved fund balance available for spending at the government's discretion within the purposes specified for the County's funds.
- At the end of 2010 the unreserved, undesignated fund balance for the General Fund was \$67.6 million, amounting to 11.5 percent of total General Fund expenditures. Total fund balance for the General Fund increased 7.1 percent (\$5.8 million) for the year.
- The County's total bonded debt increased by 10.2 percent (\$432.3 million) in 2010 due to new bond issuance of \$509.9 million offset by \$78.7 million of debt service principal payments.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the County's basic financial statements which include three components: (1) government-wide financial statements; (2) fund financial statements; and (3) notes to the financial statements. This report also contains required supplementary information and other supplementary information in addition to the basic financial statements.

Government-wide Financial Statements

The government-wide financial statements are designed to provide readers with an overview of the County's finances in a manner similar to a private sector business. The statements provide short-term and long-term information about the County's financial position, which assists in assessing the County's financial condition at the end of the fiscal year. These statements are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. This means they follow methods that are similar to those used by most businesses, taking into account all revenues and expenses connected with the fiscal year, even if cash involved has not been received or paid. The government-wide financial statements include two statements:

The **statement of net assets** presents all of the County's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in the County's net assets may serve as a useful indicator of whether the financial position of the County is improving or deteriorating.

The **statement of activities** presents information showing how the County's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. As a result, revenues and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods, such as revenues pertaining to uncollected taxes and expenses pertaining to earned but unused vacation and sick leave.

Both of the government-wide financial statements have separate sections for three different types of County programs or activities:

Governmental activities. The activities in this section are principally supported by taxes and intergovernmental revenues. Most of the County's basic services fall into this category, including general government; law, safety and justice; physical environment; transportation; economic environment; mental and physical health; culture and recreation; and debt service. Also included within the governmental activities are the 2010 operations of the County's flood control district and ferry district. Although legally separate from the County, these component units are blended with the primary government (King County) because of their governance relationship with the County. Four Washington state nonprofit corporations, included as a single internal service fund called the Building Development and Management Corporations, are reported as a single blended component unit of the County.

Business-type activities. These functions are intended to recover all or a significant portion of their costs through user fees and charges to external users of goods and services. These business-type activities include the operation of the County's public transportation system, wastewater treatment facilities, solid waste disposal facilities, airport, and other services.

Discretely presented component units. The government-wide financial statements include not only King County itself as the primary government, but also three legally separate entities for which the County is financially accountable: the Harborview Medical Center (HMC), the Washington State Major League Baseball Stadium Public Facilities District (PFD), and the Cultural Development Authority (CDA) of King County. Individual financial statements for HMC, the PFD, and the CDA can be found immediately following the fiduciary funds financial statements in the Basic Statements section of this report.

Fund Financial Statements

The fund financial statements are designed to report information about groupings of related accounts used to maintain control over resources that have been segregated for specific activities or objectives. The County, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the County can be divided into three categories: **governmental** funds, **proprietary** funds, and **fiduciary** funds.

Governmental funds. Most of the services provided by the County are accounted for in governmental funds. Governmental funds are used to account for essentially the same functions that are reported as governmental activities in the government-wide financial statements. Unlike the government-wide financial statements, however, the governmental funds financial statements focus on how cash and other financial assets can readily be converted to available resources, and the balances left at year-end that are available for future spending. Such information may be useful in determining whether there will be adequate financial resources available to meet the current needs of the County.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental funds balance sheet and the governmental funds statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The County maintains a general fund and several other individual governmental funds organized according to their type (special revenue, debt service, and capital projects). Two governmental funds, the General Fund and the Public Health Fund, are considered to be major funds for financial reporting purposes. Each of the major funds is presented in a separate column in the governmental funds balance sheet and the governmental funds statement of revenues, expenditures, and changes in fund balances. Data from the other governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these nonmajor funds is provided in the form of combining statements in the Governmental Funds section of this report, following the Basic Statements section.

The County adopts an annual budget appropriated at the department or division level for the General Fund and at the fund level for the Public Health Fund. A budgetary comparison statement has been provided for each of the two major governmental funds.

The basic governmental funds financial statements can be found immediately following the government-wide statements.

Proprietary funds. Proprietary funds are used to account for services for which the County charges customers a fee. Proprietary funds provide the same type of information as shown in the government-wide financial statements, only in more detail. Like the government-wide financial statements, proprietary funds financial statements use the accrual basis of accounting. The basic proprietary funds financial statements can be found immediately following the governmental funds financial statements.

The County maintains two types of proprietary funds:

Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The proprietary funds financial statements provide separate information for the Water Quality Enterprise and the Public Transportation Enterprise, both considered to be major funds of the County for financial reporting purposes. All other enterprise funds are aggregated into a single presentation within the proprietary funds financial statements.

Internal service funds are used to report activities that provide services to the County's other programs and activities on a cost reimbursement basis. The County uses internal service funds to account for its motor pool, information and telecommunications services, facilities management, risk management, employee benefits, building development and construction, and financial and various other administrative services. These services predominantly benefit governmental rather than business-type functions and have been included within governmental activities in the government-wide financial statements. One internal service fund that provides equipment and fleet maintenance and procurement for the Water Quality Enterprise is included within the business-type activities in the government-wide financial statements but is combined with all other internal service funds into a single aggregated presentation in the proprietary funds financial statements.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds include the investment trust funds, used to report investment activity conducted by the County on behalf of legally separate entities, such as special districts and public authorities that are not part of the County's reporting entity, and the agency funds. Since the resources of these funds are not available to support the County's own programs, they are not reflected in the government-wide financial statements. The accounting for fiduciary funds is much like that used for proprietary funds. The basic fiduciary funds financial statements can be found immediately following the proprietary funds financial statements.

Notes to the financial statements

The notes provide additional information essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found immediately following the individual component unit financial statements in the Basic Statements section of this report.

Other information

Required supplementary information. In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information on infrastructure assets reported using the modified approach. The required supplementary information immediately follows the notes to the financial statements in the Basic Statements section of this report.

Combining Statements. The combining statements are presented in separate sections immediately following the required supplementary information.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Analysis of Net Assets

An analysis of net assets may serve as a useful indicator of a government's financial position. As indicated in the condensed financial information below, derived from the government-wide Statement of Net Assets, the County's combined net assets (governmental and business-type activities) were \$4,415.3 million at the end of 2010. This is an increase of 2.5 percent (\$108.9 million) over the net assets of the previous year, as restated.

Governmental activities. Although net assets of the County's governmental activities increased 3.5

percent (\$73.7 million) to \$2,161.7 million, all of the net assets are either subject to external restrictions as to how they may be used, or are invested in capital assets (e.g., land, buildings, infrastructure, rights-of-way, equipment, and work in progress) less any related outstanding debt used

to acquire those assets. Consequently, unrestricted net assets for governmental activities showed a \$228.6 million deficit at the end of 2010. This is a \$47.6 million decrease in the deficit in unrestricted net assets from the end of 2009.

	Net Assets (in thousands)					
	Governmental Activities		Business-type Activities		Total	
	2010	2009	2010	2009	2010	2009
Assets						
Current and other assets	\$ 1,117,901	\$ 1,004,062	\$ 1,244,205	\$ 1,173,751	\$ 2,362,106	\$ 2,177,813
Capital assets	2,729,811	2,685,400	5,218,405	4,869,586	7,948,216	7,554,986
Total Assets	3,847,712	3,689,462	6,462,610	6,043,337	10,310,322	9,732,799
Liabilities						
Long-term liabilities	1,426,970	1,406,265	3,840,465	3,477,342	5,267,435	4,883,607
Other liabilities	259,087	195,239	368,537	347,584	627,624	542,823
Total Liabilities	1,686,057	1,601,504	4,209,002	3,824,926	5,895,059	5,426,430
Net Assets						
Invested in capital assets, net of related debt	1,922,455	1,889,721	1,577,670	1,603,232	3,500,125	3,492,953
Restricted	467,772	474,425	259,357	649,948	727,129	1,124,373
Unrestricted	(228,572)	(276,188)	416,581	(34,769)	188,009	(310,957)
Total net assets	\$ 2,161,655	\$ 2,087,958	\$ 2,253,608	\$ 2,218,411	\$ 4,415,263	\$ 4,306,369

This deficit does not mean that the County's governmental activities do not have resources available to pay their obligations in the coming year. The increase in net assets for governmental activities in 2010 reflects the County's ability, on an annual basis, to meet its current obligations in those activities including the related debt service requirements. The deficit in unrestricted net assets is the result of the governmental activities having long-term commitments that are greater than currently available resources. Specifically, the County's governmental activities include general obligation debt of \$291.5 million, \$30.5 million less than at the end of 2009, for which no corresponding assets are recorded but for which future revenues are obligated.

Of the amount of debt with no corresponding assets, 65.5 percent (\$190.8 million) is related to assets recorded on the books of two of the County's three discretely presented component units: the Washington State Major League Baseball Stadium PFD (\$51.2 million), and the Harborview Medical Center (\$139.6 million). As discretely presented component units, these entities are not part of the primary government or incorporated into this

analysis. The remaining debt consists of \$80.2 million associated with the Kingdome facility, demolished in 2000, and \$20.5 million used to finance assets that have been contributed by the County to other programs and services that benefit the citizens of the County.

Business-type activities. There was an increase of 1.6 percent to \$2,253.7 million in the net assets of business-type activities. Of the total net assets for business-type activities, 70.0 percent (\$1,577.7 million) is invested in capital assets (e.g., land, buildings, vehicles, plant assets, equipment, and work in progress), net of related debt. The business-type activities use these capital assets to provide services to their customers; consequently, these assets are not available for future spending. The resources needed to repay the debt incurred to acquire these assets must be provided from other sources since the capital assets themselves cannot be liquidated for these liabilities. Another 11.5 percent of the total net assets of business-type activities is restricted for capital construction (\$10.1 million), debt service (\$215.6 million), regulatory assets and environmental liabilities (\$30.3 million) and for other purposes (\$3.4

million). The remaining 18.5 percent (\$416.6 million) is unrestricted net assets. Any balance in the unrestricted net assets for business-type activities cannot be used to reduce the unrestricted net asset deficit in governmental activities.

The combination of the \$228.6 million deficit in the governmental activities unrestricted net assets and the \$416.6 million positive balance in the business-type activities unrestricted net assets resulted in a net positive \$188.0 million in total unrestricted net assets for the County as a whole.

Analysis of Changes in Net Assets

The increase in the County's total net assets in 2010 resulted from revenues exceeding related expenses and reflects the County's ability to meet its ongoing obligations, including its debt service requirements. Approximately 42.6 percent of the County's total revenues came from taxes, primarily Property taxes and the Retail sales and use taxes. Charges for various goods and services provided 43.1 percent of the total revenues, while 13.7 percent was derived from operating and capital grants and contributions, including state and federal assistance. The County's expenses cover a range of services, the largest of which were for law, safety and justice; mental and physical health; public transportation; and water quality.

The condensed financial information on the following page is derived from the government-wide Statement of Activities and reflects how the County's net assets changed during 2010.

Governmental activities. Governmental activities accounted for 67.7 percent of the total growth in net assets of the County, resulting in an increase in

the County's governmental activities net assets of \$73.7 million. Program revenues for governmental activities total \$884.3 million and include the amount paid by those who directly benefit from the programs (\$573.2 million), and by other governments and organizations that subsidized certain programs with operating grants and contributions (\$198.5 million), and capital grants and contributions (\$112.5 million). In 2010, the cost of all governmental activities was \$1,651.1 million. The County paid for the \$766.8 million remaining public benefit portion of governmental activities with \$593.1 million in property taxes, \$180.9 million in retail sales and use taxes, and \$64.1 million in other revenues, including other taxes and interest earnings. As discussed earlier, all of the increase in governmental activities net assets was either restricted as to use or used to acquire capital assets for use in providing services.

The growth in net assets of governmental activities of \$73.7 million is primarily due to the following factors: the collection of revenues (mostly taxes) to fund repayments of long-term debt (\$62.9 million), the collection of revenues for the acquisition of capital assets (\$58.9 million), donations of capital assets, primarily infrastructure, to the county (\$82.8 million), taxes collected by Special Revenue Funds (\$8.6 million by Emergency Medical Services, \$8.5 million by the Flood Control District, and \$3.6 million by the Mental Health Fund) in excess of the services provided in 2010 (\$20.7 million). In addition, the book value of capital assets sold, retired, or transferred (\$116.0 million) and depreciation expense (\$32.2 million) reduced net assets.

Changes in Net Assets (in thousands)						
	Governmental Activities		Business-type Activities		Total	
	2010	2009	2010	2009	2010	2009
Revenues						
Program revenues						
Charges for services	\$ 573,209	\$ 571,653	\$ 666,574	\$ 632,427	\$ 1,239,783	\$ 1,204,080
Operating grants and contributions	198,512	206,826	57,514	90,570	256,026	297,396
Capital grants and contributions	112,530	75,592	26,220	38,020	138,750	113,612
General revenues						
Property taxes	593,135	624,448	22,174	-	615,309	624,448
Retail sales and use taxes	180,914	179,077	375,943	376,968	556,857	556,045
Other taxes	53,760	54,234	-	-	53,760	54,234
Unrestricted interest earnings	10,295	20,029	8,810	13,558	19,105	33,587
Total revenues	<u>1,722,355</u>	<u>1,731,859</u>	<u>1,157,235</u>	<u>1,151,543</u>	<u>2,879,590</u>	<u>2,883,402</u>
Expenses ^(a)						
General government ^(b)	193,521	106,076	-	-	193,521	106,076
Law, safety and justice	605,396	607,191	-	-	605,396	607,191
Physical environment	79,897	76,404	-	-	79,897	76,404
Transportation	108,386	117,625	-	-	108,386	117,625
Economic environment	103,153	105,515	-	-	103,153	105,515
Mental and physical health	456,678	458,184	-	-	456,678	458,184
Culture and recreation	54,071	53,313	-	-	54,071	53,313
Interest and other debt service costs	49,979	54,010	-	-	49,979	54,010
Airport	-	-	22,296	24,725	22,296	24,725
Public transportation	-	-	697,611	673,436	697,611	673,436
Solid waste	-	-	101,210	91,347	101,210	91,347
Water quality	-	-	290,873	287,792	290,873	287,792
Other enterprises activity	-	-	7,625	7,153	7,625	7,153
Total expenses	<u>1,651,081</u>	<u>1,578,318</u>	<u>1,119,615</u>	<u>1,084,453</u>	<u>2,770,696</u>	<u>2,662,771</u>
Increase in net assets before transfers	71,274	153,541	37,620	67,090	108,894	220,631
Transfers	2,423	896	(2,423)	(896)	-	-
Increase in net assets	<u>73,697</u>	<u>154,437</u>	<u>35,197</u>	<u>66,194</u>	<u>108,894</u>	<u>220,631</u>
Net assets, beginning of year (restated) ^(c)	<u>2,087,958</u>	<u>1,933,521</u>	<u>2,218,411</u>	<u>2,152,217</u>	<u>4,306,369</u>	<u>4,085,738</u>
Net assets, end of year	<u>\$ 2,161,655</u>	<u>\$ 2,087,958</u>	<u>\$ 2,253,608</u>	<u>\$ 2,218,411</u>	<u>\$ 4,415,263</u>	<u>\$ 4,306,369</u>

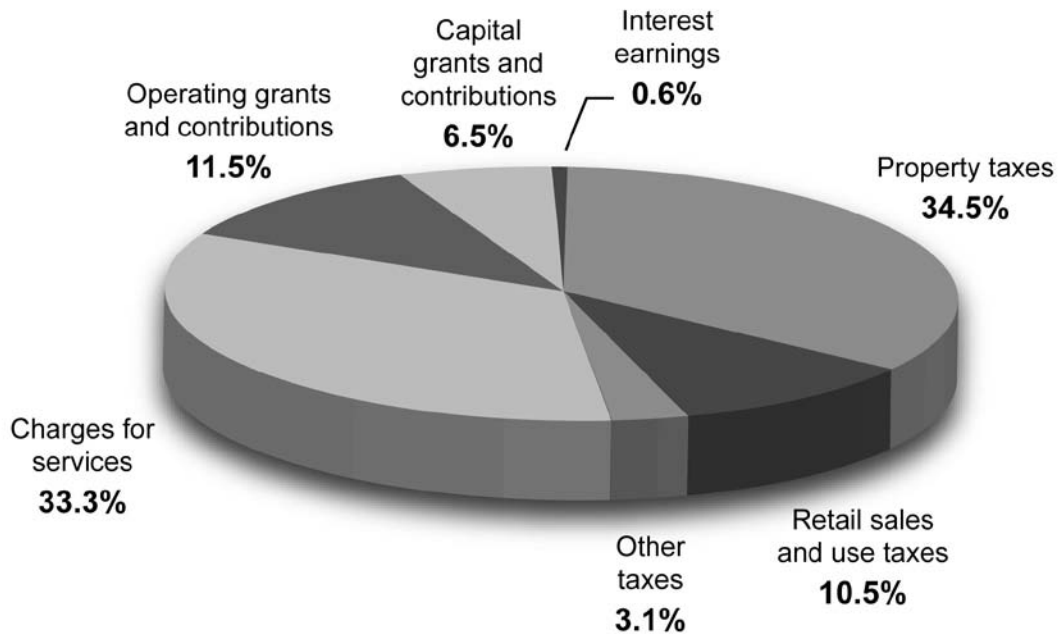
(a) Expenses for all functions include the allocation of indirect expenses from the general government function. The amount of indirect general government expenses allocated to each function is shown in a separate column on the County's government-wide Statement of Activities alongside the column that reflects the direct operating expenses incurred by each function. As a result of this allocation, the \$193.5 million in General government expense above consists of \$135.9 million in direct program expenses and loss on the disposal (transfer) of capital assets of \$116.1 million reduced by a net allocation of \$58.5 million to other County functions.

(b) General government expenses includes loss on sale/disposal/transfer of capital assets of \$116.1 million and \$36.5 million in 2010 and 2009, respectively.

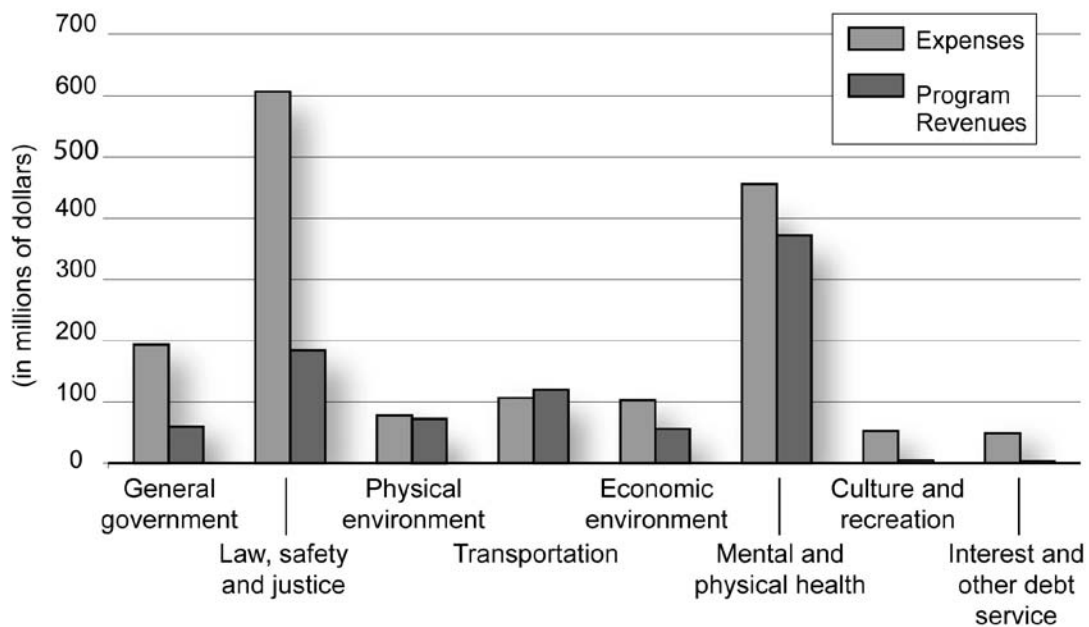
(c) Net assets, beginning of year has been restated, see Note 17 - "Restrictions, Reserves, Designations, and Changes in Equity" – Restatements of Beginning Balances.

The charts below illustrate the County's revenues by source and its expenses and program revenues by function for its governmental activities:

Revenues by Source — Governmental Activities 2010



Expenses and Program Revenues — Governmental Activities 2010



Charges for services provided 33.3 percent, and property taxes 34.5 percent, of total revenues for governmental activities. One of the most significant expense amounts is for Law, safety and justice, a function that requires the greatest usage of general government revenues. The primary revenue sources for Mental and physical health are charges for services and operating grants and contributions, which paid for 81.8 percent of the activities of that

function. In 2010, Transportation received \$82.1 million in infrastructure and right-of-way capital assets from developers, which enabled program revenues to exceed expenses by \$13.0 million. These and other capital contributions accounted for 112.3 percent of the 2010 increase in governmental activities net assets.

A comparison of the cost of services by function for the County's governmental activities, along with the revenues used to cover the net expenses of the governmental activities (in thousands):

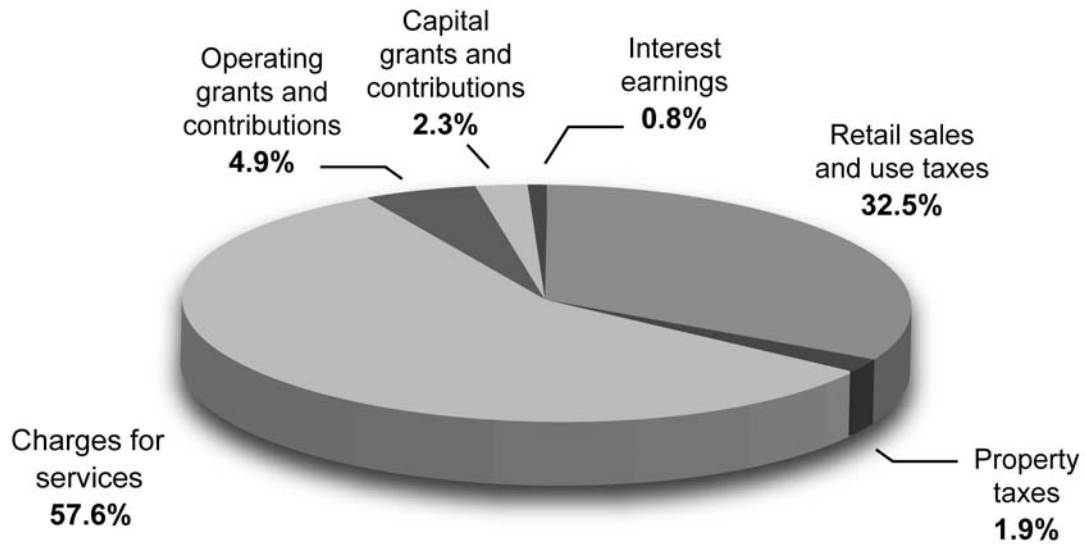
(Expenses) Net of Program Revenues	
General government	\$ (134,359)
Law, safety and justice	(420,086)
Physical environment	(6,467)
Transportation	12,972
Economic environment	(44,232)
Mental and physical health	(83,790)
Culture and recreation	(47,001)
Interest and other debt service costs	(43,867)
Total expenses	(766,830)
General revenues	
Property taxes	593,135
Retail sales and use taxes	180,914
Other taxes	53,760
Unrestricted interest earnings	10,295
Transfers from Business-type	2,423
Increase in net assets	<u>\$ 73,697</u>

Business-type activities. Business-type activities increased the County's net assets by \$35.2 million in 2010, accounting for 32.3 percent of the total growth in net assets of the County. Total revenues for business-type activities were \$1,157.2 million. The cost of all business-type activities for 2010 was \$1,119.6 million. Of that amount, 67.0 percent (\$750.3 million) was funded from program revenues, including \$666.6 million in charges for services, \$57.5 million from other governments and

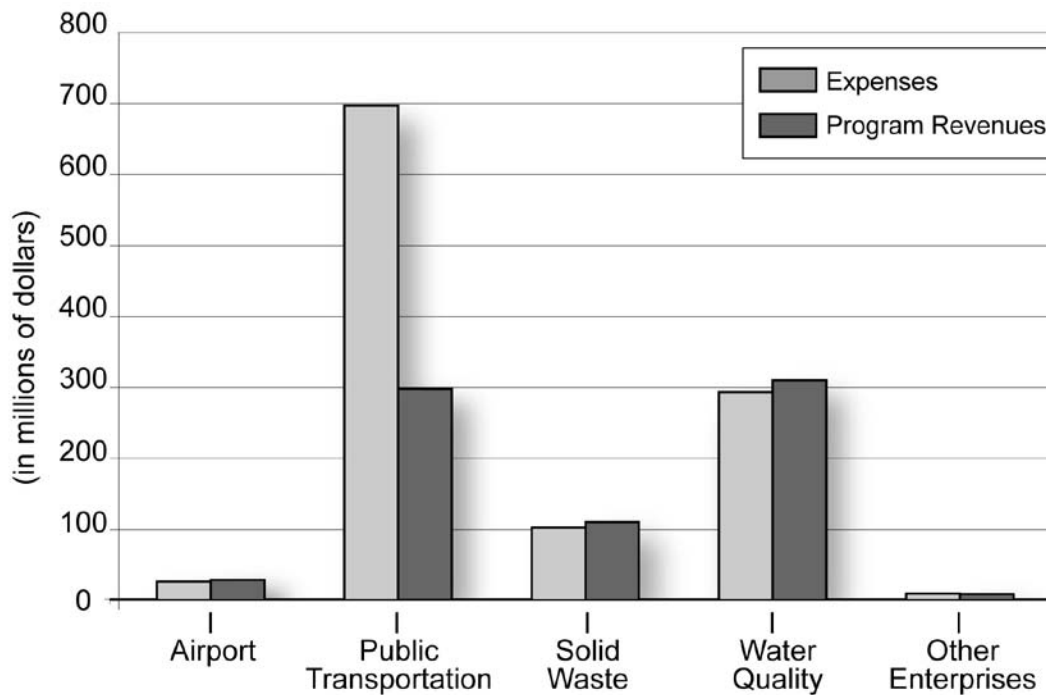
organizations that subsidized certain programs with operating grants, and \$26.2 million in capital grants and contributions. The Public Transportation operations are subsidized by retail sales and use tax revenues, which amounted to \$375.9 million in 2010 and property taxes (beginning in 2010) of \$22.2 million. In addition, business-type activities earned \$8.8 million in unrestricted interest earnings.

Business-type revenues by source and business-type expenses and program revenues by function:

Revenues by Source — Business-type Activities 2010



Expenses and Program Revenues — Business-type Activities 2010



FINANCIAL ANALYSIS OF THE COUNTY'S FUNDS

The County uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds

The focus of the County's governmental funds is to provide information on near-term inflows, outflows, and balances of resources that are available for spending. Such information is useful in assessing the County's financing requirements. Unreserved fund balances may serve as a useful measure of a government's net financial resources available for spending at the end of the fiscal year.

As of December 31, 2010, the County's governmental funds reported combined ending fund balances of \$565.4 million, an increase of \$43.7 million in comparison with the prior year. Approximately 80.3 percent (\$453.9 million) constitutes unreserved fund balance available for spending in the coming year at the County's discretion. The remainder of fund balance is reserved to indicate that it is not available for new spending because it has already been committed to the liquidation of outstanding contracts and purchase orders of the prior fiscal year (\$60.8 million), to pay debt service (\$24.2 million), for prepayments (\$8.1 million), and for a variety of other restricted purposes (\$17.9 million).

Overall governmental fund revenues totaled approximately \$1,719.5 million for 2010, which represents a decrease of 1.6 percent, (\$28.2 million), under the fiscal year ended December 31, 2009. While Retail sales and use taxes were up \$1.8 million, Intergovernmental revenues were up \$16.6 million, and Miscellaneous revenue increased \$4.7 million, while several other revenue categories had sharp declines. Property taxes were down \$28.7 million due to declines in collections for the King County Ferry District (down \$17.7 million due to a decrease in the levy rate), Unlimited Tax GO Bonds (down \$13.9 million due to a decrease in the levy rate), the County Road Fund (down \$3.2 million due to annexations), the Emergency Medical Services Fund (down \$2.4 million due to a decrease in the assessed value of taxable property) and the Automated Fingerprint Identification System (down \$1.6 million due to a decrease in the assessed value of taxable property).

In 2010, expenditures for governmental funds totaled \$1,762.9 million, a decrease of 3.8 percent (\$69.4 million) from the previous fiscal year. Current expenditures were down 2.1 percent (\$33.1 million) from the previous fiscal year due to programmatic reductions with the priority of the preservation of funding for core mandatory services over discretionary services. Debt service expenditures (excluding the payment to escrow agent) were down \$60.5 million (38.9 percent), and Capital outlay expenditures were up \$30.2 million (35.5 percent). Total expenditures for governmental funds exceeded revenues by \$43.3 million in 2010, compared to \$84.5 million for 2009. The change in fund balances in 2010 of \$43.7 million included a increase of \$10.4 million in Non-major Debt Service Funds and an increase of \$38.6 million in Capital Projects Funds.

The **General Fund** is the primary operating fund for the County. At the end of the fiscal year, total fund balance for the General Fund was \$88.2 million. Unreserved fund balance, the amount considered available to spend, totaled \$71.6 million. Of that amount, \$4 million has been designated and is not considered available to spend. As a measure of the General Fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved fund balance represents 12.2 percent of total General Fund expenditures, an increase from the 11.4 percent of a year ago. Total fund balance represents 15.1 percent of total General Fund expenditures, an increase from the 13.9 percent of a year ago.

The fund balance of the County's General Fund increased \$5.8 million during 2010, while the fund balance decreased in 2009 by \$9.7 million (an increase of over \$15 million). While revenues were down \$3.6 million (0.6 percent) in 2010, expenditures declined \$7.3 million (1.2 percent) and Other financing uses declined \$12.9 million. While property tax revenues increased by \$6.2 million and intergovernmental revenues were up \$7.6 million, charges for services were down \$12.5 million and interest earnings were down \$5.9 million, resulting in the net increase in revenues in 2010 from the 2009 level of \$3.6 million. Expenditures were down \$7.3 million due to reductions in expenditures for general government services (\$4.6 million) and mental and physical health (\$3.4 million). The large drop in Other financing uses of \$12.9 million is due to

substantially decreased transfers from the General Fund to human services programs.

The **Public Health Fund** is used to account for health service centers located throughout the County and other public health programs that promote health and prevent disease to King County residents. At the end of 2010 it had a total fund balance of \$7.4 million (up \$3.1 million in 2010), of which \$5.8 million was unreserved and available for spending. While revenues were up \$7.1 million in 2010 from the 2009 level (due to an increase of \$7.5 million in intergovernmental revenues) expenditures were essentially unchanged in 2010 and other financing sources were down \$4.0 million resulting in an increase in fund balance of \$3.1 million in 2010 versus a decrease of \$44 thousand in 2009.

Proprietary Funds

The County's proprietary funds provide the same type of information found in the government-wide financial statements for business-type activities. This information is presented on the same basis of accounting, but provides more detail.

The County's net assets increased by \$35.2 million as a result of operations in the proprietary funds, adjusted to reflect the consolidation of internal service fund activities related to the enterprise funds. Of the two major proprietary funds, the Public Transportation Enterprise had an increase of \$0.5 million and the net assets of the Water Quality Enterprise increased by \$18.6 million. In 2010, net assets of the Solid Waste Enterprise increased by \$9.4 million.

The **Public Transportation Enterprise** accounts for the operations, maintenance, capital improvements, and expansion of public transportation and related facilities in the County. At the end of 2010 the Public Transportation Enterprise had total net assets of \$1,454.6 million of which 66.2 percent (\$962.6 million) was invested in capital assets, net of related debt; 1.7 percent (\$24.9 million) was restricted as to use for capital purposes, bond reserves, and other purposes; and 32.1 percent (\$467.1 million) was unrestricted and available for spending. Net assets increased in 2010 and 2009. The increase was \$0.5 million in 2010 and \$29.4 million in 2009. The change in 2010 is primarily attributed to an increase in cash balances held for future capital investments that are currently projected to occur over the next few years, as well as debt service, which was offset by a decrease in non-depreciating capital assets as

constructed assets were moved into service and began depreciating. On December 31, 2010, cash balances were used to support interfund loans of \$116.1 million to other County agencies. At the end of 2009, interfund loans to other County agencies totaled \$131.5 million. The reserve for future fleet replacement continued to be replenished consistent with existing policies and in anticipation of upcoming fleet replacements.

The **Water Quality Enterprise** accounts for the operations, maintenance, capital improvements, and expansion of the County's water pollution control facilities. Total net assets in the Water Quality Enterprise were \$562.4 million at the end of 2010 of which 72.4 percent (\$407.2 million) was invested in capital assets, net of related debt; 41.7 percent (\$234.4 million) was restricted for debt service and regulatory assets and environmental liabilities; and the remaining negative 14.1 percent (\$79.2 million) was unrestricted. Water Quality operating revenues decreased by 0.7 percent to \$304.8 million, while operating expenses net of depreciation increased by 0.6 percent to \$103.7 million. Water Quality collected a monthly sewage treatment charge of \$31.90 per Residential Customer Equivalents (RCE) in 2010 and 2009. The negative unrestricted net assets balance was reduced to (\$79.2 million) at the end of 2010 from (\$88.0 million) at the end of 2009.

General Fund Budgetary Highlights

The County's final General Fund budget differs from the original budget in that it reflects an increase in appropriations of \$15.0 million during the year due to 2010 supplemental budget appropriations for General Fund support for general government (\$2 million), law, safety and justice (\$4 million), physical environment (\$2.5 million), and transfer to support capital projects (\$5.9 million). However, actual budgetary basis expenditures (including encumbrances) were only \$61 thousand greater than the original budget. This resulted in an underutilization of the total final appropriation authority by less than \$15 million, including \$5.7 million of under-expenditures in General government services, \$2.6 million in Law, safety and justice, and \$5.6 million in Transfers out. During the year total budgetary basis revenues were greater than budgetary estimates by \$10.4 million with a net impact of increasing fund balance by \$5.8 million in 2010.

CAPITAL ASSETS, INFRASTRUCTURE, AND DEBT ADMINISTRATION

Capital assets

The King County primary government's investment in capital assets for its governmental and business-type activities as of December 31, 2010, amounts to \$7.9 billion (net of accumulated depreciation). Capital assets include land, rights-of-way, easements and development rights, buildings, improvements other than buildings, roads and bridges infrastructure, vehicles, machinery, computers, software and other equipment, and construction work-in-progress. The total increase in the investment in capital assets over the previous year was 5.1 percent (1.7 percent increase for governmental activities and 7.1 percent increase for business-type activities).

Major capital asset events during 2010 included the following:

- Construction continued on the new Brightwater Treatment Plant and the associated conveyance system. This project comprised the bulk of the 19 percent increase

in business-type work-in-progress during the year. Construction activities are simultaneously ongoing in the treatment plant, the conveyance systems (portals and conveyance pipes), and ancillary facilities. The treatment plant is scheduled for completion and to begin operations in 2011 with the conveyance systems to be completed in 2012.

- Significant construction activity is also occurring in the Public Transportation and Solid Waste enterprises. Public Transportation continued to make improvements at bus bases, transit centers, and park-and-ride facilities. The Solid Waste Enterprise continued to make improvements to existing transfer stations and development of landfill ancillary systems.
- For governmental activities, significant additions and upgrades were made to parks facilities, development and improvements to the trail system, renovations and upgrades to various county buildings, and technology-related projects.

A summary of the 2010 capital assets activity is shown below. More detailed information on the County's capital assets can be found in Note 6 – "Capital Assets."

	Capital Assets (in millions)					
	Governmental Activities		Business-type Activities		Total	
	2010	2009	2010	2009	2010	2009
Land and land rights	\$ 859.8	\$ 798.8	\$ 360.8	\$ 358.3	\$ 1,220.6	\$ 1,157.1
Buildings*	731.0	731.7	1,008.5	1,012.1	1,739.5	1,743.8
Improvements other than buildings*	50.9	27.1	496.4	497.7	547.3	524.8
Infrastructure - roads and bridges	925.4	943.1	0.0	0.0	925.4	943.1
Infrastructure - other*	5.3	0.0	728.3	709.0	733.6	709.0
Equipment and software*	78.6	77.9	515.5	525.8	594.1	603.7
Construction in progress	78.8	106.8	2,108.9	1,766.5	2,187.7	1,873.3
Total	<u>\$ 2,729.8</u>	<u>\$ 2,685.4</u>	<u>\$ 5,218.4</u>	<u>\$ 4,869.4</u>	<u>\$ 7,948.2</u>	<u>\$ 7,554.8</u>

* Net of depreciation/amortization

Infrastructure

The County has elected to use the modified approach in reporting roads and bridges. Under the modified approach, asset condition is reported rather than recording depreciation. The rating scales for pavements (roads) and bridges are further explained in the required supplementary information which follows the notes to the basic financial statements.

The County performs condition assessments on its network of roads through the King County Pavement Management System, which generates a Pavement Condition Index (PCI) for each segment of arterial and local access road in the network. The PCI is a numerical index on a 100-point scale that represents the pavement's functional condition based on the quantity, severity, and type of visual distress. Condition assessments are undertaken every three years.

It is the policy of the King County Road Services Division to maintain at least 80.0 percent of the road system at a PCI of 40 or better. In the most recent condition assessments, 74.2 percent of the arterial roads in the County and 78.5 percent of the local access roads in the County had a PCI rating at 40 and above. The 2010 condition assessment indicates the arterial and local access road networks have fallen below the 80/40 threshold. The County's Roads Division's current budget conditions do not allow for additional funds to increase the number of miles overlaid. The accelerated condition of deterioration observed between the 2009 and 2010 reports are primarily the result of weather and system age. The majority of roads that fall below the established rating are local access roads that are situated in rural areas. The amount budgeted in 2010 for road preservation and maintenance was \$78.8 million. The amount actually expended was \$52.9 million.

Underspending of the budgeted amount is a result of the removal of roads from the project list because of conflicts with anticipated utility work, cost efficiencies related to relatively few roads to be resurfaced in remote locations, and fewer weather-related work reductions or stoppages.

The County currently maintains 180 bridges. Physical inspections to uncover deficiencies are carried out at least every two years and documented. There is also an annual evaluation to determine which bridges are due for replacement or rehabilitation using a 10-point priority scale based on various factors of bridge condition. A key element in the priority scale is the sufficiency rating, which is a numerical rating (on a 100-point scale) of a bridge based on its structural adequacy and safety, essentiality for public use, and its serviceability and functional obsolescence. The policy of the King County Road Services Division is to maintain bridges in such a manner that no more than 12 (6.5 percent) will have a sufficiency rating of 20 or less. The most current complete assessment showed 6 bridges at or below this threshold. The amount budgeted in 2010 for bridge preservation and maintenance was \$19.8 million, while the actual amount expended was \$9.7 million. Underspending of the budgeted amount is due to the construction schedule of certain projects extending beyond the budget year.

Debt Administration

At the end of 2010, King County Primary Government has a total of \$4,673.3 million in bonds and notes outstanding for its governmental and business-type activities. Of this amount, \$2,239.9 million is comprised of debt backed by the full faith and credit of the County. The \$2,433.4 million remainder of the County's debt represents bonds secured solely by specified revenue sources.

	Outstanding Debt (in millions)					
	Governmental Activities		Business-type Activities		Total	
	2010	2009	2010	2009	2010	2009
General obligation bonds	\$ 728.4	\$ 724.3	\$ 1,031.2	\$ 919.7	\$ 1,759.6	\$ 1,644.0
General obligation bond anticipation notes	84.3	27.1	-	-	84.3	27.1
Lease revenue bonds	396.0	402.5	-	-	396.0	402.5
Revenue bonds	-	-	2,433.4	2,167.4	2,433.4	2,167.4
Total	\$ 1,208.7	\$ 1,153.9	\$ 3,464.6	\$ 3,087.1	\$ 4,673.3	\$ 4,241.0

Lease revenue bonds were bonds issued in accordance with the provisions of Revenue Ruling 63-20 and Revenue Procedure 82-26. Under the lease agreements, the County's obligation to pay rent is a limited tax general obligation.

The total debt increased over the previous year by 10.2 percent or \$432.3 million (a 4.8 percent or \$54.8 million increase for governmental activities and 12.2 percent or \$377.5 million increase for business-type activities). The increase of debt outstanding in governmental activities was primarily due to the issuance of \$82.5 million of limited general obligation bonds in 2010. Business-type activities' debt increased primarily due to the issuance of \$334.4 million of sewer revenue and refunding bonds and \$100 million of Multi-Modal limited general obligation bonds payable by sewer revenues to finance the capital needs of the Water Quality Enterprise.

During 2010, the County refinanced some of its existing debt to take advantage of favorable interest rates. The County refinanced \$26.6 million of general obligation various purpose bonds which will decrease future aggregate debt service payments by \$3.3 million over the life of the bonds. The County also refinanced \$19.8 unlimited general obligation bonds which will decrease future aggregate debt service payments by \$2.2 million over the life of the bonds.

Using excess proceeds from special taxes and revenues, the County completed a partial defeasance of general obligation (baseball stadium) bonds that is expected to decrease debt service payments by \$15.0 million.

The County maintains a rating of "Aa1" from Moody's, a rating of "AAA" from Standard & Poor's, and a rating of "AA+" from Fitch for its limited tax general obligation debt. For its unlimited tax

general obligation debt the County has a rating of "Aaa" from Moody's, a rating of "AAA" from Standard & Poor's, and a rating of "AAA" from Fitch. The ratings for Water Quality Enterprise's revenue debt are "Aa2" from Moody's and "AA+" from Standard & Poor's.

State statutes limit the amount of general obligation debt that the County may issue to 2.5 percent of its total assessed valuation for general county purposes and 2.5 percent for metropolitan functions. The current debt limitation of total general obligations for general county purposes is \$8,260.4 million, significantly higher than the County's outstanding net general obligation long-term liabilities of \$1,139.2 million. For metropolitan functions the debt limitation is \$8,260.4 million and the County's outstanding net general obligation debt is \$1,079.1 million.

Additional information on King County's long-term debt can be found in Note 14 – "Debt."

ECONOMIC OUTLOOK AND 2011 BUDGET

Economic factors have a direct impact on the County's revenues and the demand for services. The County's revenue sources include taxes, charges for services, and intergovernmental revenues. The largest single source is taxes, which comprise approximately one-third of total revenues and consist primarily of taxes on real property. Property taxes tend to be stable because the County establishes assessed value from the preceding four years of real estate sales. Other tax

sources, such as retail sales tax, are more volatile and directly influenced by economic conditions in the region.

Property assessed valuation in 2010 for taxes collected in 2011 decreased by 11.6 percent compared to increases of 13.5 percent and 14.1 percent in 2009 and 2008, respectively. Unemployment in King County was 8.8 percent in 2010 compared with 8.5 percent in 2009. Median household income in the county is estimated to have decreased 2.9 percent from 2008 to 2009 and decreased 2.9 percent from 2009 to 2010. County taxable sales decreased in both 2009 and 2010, affecting several funds, most notably the General Fund and Public Transportation Fund.

By law, the County is required to adopt a balanced budget. The 2011 budget, adopted by the County Council in November 2010, totals \$5.0 billion, which includes annual, biennial, and the current year portion of multi-year capital improvement budgets. Of this amount, \$629.2 million is appropriated for the General Fund; \$1.8 billion (\$393.7 million annual and \$1,407.4 million biennial) is appropriated for enterprise funds including public transportation, solid waste and wastewater treatment; and \$1.16 billion (\$892.8 million annual and \$271.5 million biennial) is appropriated for special revenue funds including public health, mental health, emergency medical services, human services, and road funds. The budget also includes \$751.4 million committed to capital improvements for wastewater treatment, transit, roads, solid waste and other major public facilities. The general fund current expense budget maintained a 6.0 percent budgetary undesignated fund balance as a percentage of revenues.

Other considerations

King County will continue to face numerous challenges, including volatile energy prices, rising employee and programmatic health care costs, the cost of providing services to urban unincorporated areas, and the need to raise sufficient revenues to support utility, transit system and general government activities.

Property taxes are the largest revenue source in the County general fund at 40 percent of general fund revenues. The County Council-approved property tax levy is limited by state law to one percent growth each year plus the property tax on new construction.

Three large annexations become effective in 2010 and 2011. Effective April 1, 2010, the southern portion of North Highline became part of the City of Burien. In July 2010, the Panther Lake area became part of the City of Kent, and effective July 1, 2011, the Juanita, Finn Hill and Kingsgate areas will become part of the City of Kirkland.

REQUESTS FOR INFORMATION

This financial report is designed to provide an overview of the County's financial activities for all those with an interest in the government's finances. Questions concerning any of the information provided in this report, or requests for additional financial information, should be addressed to the Chief Accountant, 500 Fourth Avenue Room 653, Seattle, WA 98104.

